

# Accounting Report

## Financial Reporting Council (FRC) Meeting

**A** regular meeting of the Financial Reporting Council (FRC) took place on February 13, 2002. The results of the meeting were presented to the Standards Advisory Council (SAC) at IASC Board. The SAC meeting was held in London on 18 – 19 February 2002.

Besides the organizational part the following issues were discussed during the FRC meeting:

- Certain aspects of the IASC Board projects on the *Improvement of the Existing IFRS* and *First Application of IFRS*, that had been brought for discussion by the Board during the SAC meeting in February of 2002;
- Procedures and composition of the working group on Financial Reporting in extractive industries that was established in accordance with the FRC decision at its previous meeting in December of 2001;
- Amendments to the Provisional FRC Regulation concerning the appointment of the FRC Chairperson and members, and also termination of their authorities.

A meeting of the section *International Financial Reporting Standards: application practices and perspectives in Russia* was held within the Council on Corporate Governance on 4 April 2002.



### ACCOUNTING REFORM PROGRESS

Representatives of companies that prepare financial reporting in compliance with IFRS, professional participants of the securities market and auditors participated in the meeting.

Necessity to transfer to the reporting according to IFRS was repeatedly discussed at high-ranking meetings, within the professional community and mass media. Any investor is primarily interested in obtaining adequate and fair information about the object of his investment. Unfortunately, today information about Russian companies in many cases fails to give a clear picture. According to certain international audit companies such gaps and problems regarding disclosures happen due to the accounting standards that are lagging behind market needs very much rather than the audit itself. It should be noted that reporting data issued for «internal usage» and «for export» could

have significant differences on the same positions. For instance, profit determined in accordance with the Russian rules in many instances is transformed into losses when determined in accordance with IFRS.

Similarly, amount and type of information disclosed for foreign users may several times exceed the information contained in the reports issued for Russian shareholders and regulatory authorities (for instance, in accordance with the IFRS it is required to provide detailed disclosure of transactions with affiliates, i.e. related parties).

Notwithstanding the fact that the Government does not provide direct support with respect to application of IFRS, a number of Russian companies have been using them for a long time already, and some companies intend to apply the standards. In the process of practical IFRS usage Russian companies face problems, which could be defined as following:

1. Double costs burden in case of reporting under the Russian standards and IFRS; with adoption of chapter 25 of the Tax Code of the Russian Federation the burden has tripled, since the reporting requirements for taxation purposes have been added.

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2. Lack of qualified personnel, lack of the market of IFRS specialists; lack of the certification program for IFRS specialists in the Russian language, IPB certification program does not include IFRS.
3. Difficulty when selecting a consultant on IFRS application as well as an auditor, inadequate IFRS specialists service market;
4. Lack of practical guidance on the IFRS application, absence of a professional body that could provide qualified consultation on IFRS application.

Based on the discussion of the above listed problems during the meeting of the section on IFRS within the Council on Corporate Governance, the participants worked out certain proposals regarding the development of a supporting mechanism for IFRS application in Russia to provide assistance both to companies that are already applying IFRS, and also Russian investors in terms of their ability to obtain reliable information prepared under IFRS from the securities market participants by means of introducing relevant requirements regarding disclosures.

Proposals of the participants of the meeting on certain directions regarding the creation of such **supporting mechanism for Russian companies in applying IFRS**, are listed below:

#### **Coverage of companies:**

1. Listed companies in the securities market or international capital markets;
2. Financial institutions (banks, professional participants of the securities market, investment funds);
3. Medium size companies that are already applying or willing to apply IFRS with intentions not related to entering the organized securities market;
4. Special purpose charitable funds.

#### **Legal support:**

To cover the first stage of IFRS implementation in Russia (for more details see below) when presenting consolidated reporting in compliance with IFRS the legal support shall include:

1. Changes and amendments to the legislation about joint-stock companies and securities market as to disclosure and consolidated reporting audit in accordance with the international standards and also in terms of securities listing requirements established by the organized market.
2. Creation of mechanism of enforcing IFRS in the Russian Federation similar to the one being established in the EU «IFRS support». Create a body consisting of specialists, however, supported by the government bodies. This is the way the European Union has chosen for its development, i.e. it established the EFRAG organization in July 2001, which has proved the necessity to involve the administrative resource to promote IFRS in the West.
3. Introduction of changes to the Auditing Law in terms of enforcing auditing of reporting prepared in compliance with IFRS.

To cover the following stages in IFRS implementation in Russia when presenting individual reporting in compliance with IFRS the legal support shall include:

1. Ability to apply IFRS as a unified basis for financial reporting for the purpose of disclosing the financial situation of a company and of its corporate events; disclosing any significant facts of its business activity, using the IFRS data, for the purpose of corporate law (net assets evaluation and dividends),
2. Legalizing of IFRS application on the matters not cur-

rently included in the Russian Accounting Regulation.

3. Introduction of changes and amendments to the accounting legislation in terms of cancellation of mandatory audit of reporting provided under the Russian regulation in instances when IFRS compliant financials are audited.
4. Settlement of the matters with regard to presenting of statistical data under IFRS to the statistical authorities.
5. Development of regulations related to the tax base on the basis of IFRS.

#### **Practical support**

Practical support implies the development of practical recommendations on IFRS application by Russian companies. Such recommendations must be based on case-studies related to Russia, prepared within the projects promoting IFRS in Russia. It is necessary to publish and enforce the official translation of IFRS into the Russian language. Both translation and recommendations on IFRS application must be revised on a regular basis.

#### **Personnel assistance implies**

1. The development of qualification requirements system for IFRS specialists including mechanism for certification of specialists;
2. The adoption of a training concept for IFRS specialists (for instance, CPA, ACCA or other programs) and the development of relevant training courses based on Russian examples.
3. The organization of a training system for specialists from investment companies and the business community in the overall on using reporting prepared in compliance with IFRS.
4. To include IFRS topics into the certification program for pro-

professional accountants provided by the Institute of Professional Accountants in Russia.

5. To develop a mechanism of recognition of international certificates for IFRS specialists (for instance, ACCA) in Russia.

### **IFRS implementation monitoring**

- The creation of assurance mechanism or IFRS implementation on the basis of professional institutions and large audit companies. Government involvement to the extent of assuring compliance with established disclosure requirements in compliance with the legislation on joint-stock companies and the securities market.
- Recent scandals with certain very large audit companies may affect the global and the Russian markets for audit services. Still remaining an administrative country Russia certainly needs «a governmental» regulatory mechanism.
- In this regard the role of FCSM must be enhanced in terms of supervising auditors' activity in the securities market. In order to ensure high professional level of regulating IFRS implementation in the securities market it is required to establish a professional body under the FCSM on the matters of practical implementation of IFRS.

### **IFRS Implementation Stages**

**First Stage.** To require all listed companies to present their consolidated reporting in compliance with IFRS (US GAAP) beginning with 2004/2005. To require from companies submitting consolidated reports according to IFRS to do so in the Russian language starting from the 2002.

**Second stage.** To allow companies to make their choice between IFRS and Russian standards for the purpose of individual company reporting. To allow those

companies that report in compliance with IFRS not to have their Russian reports been audited provided that IFRS reporting is audited.

It was also decided to set up a working group under FCSM of Russia to develop a supporting mechanism for IFRS application. Such group will be based on the FRC and the IFRS section of the Council on Corporate Governance.

*For more detailed information on the activity of the Financial Reporting Council, please, refer to the ICAR website at <http://www.icar.ru>.*

## **International Financial Reporting Standards in Russia**

*Interview with Leonid Schneidmant*

***The government's plans to introduce International Financial Reporting Standards (FRS) in Russia in 2000 were never realized. What are the chances that the transition to FRS will take place by 2005?***

This timeframe definitely appears to be more realistic. While it's relatively simple to change the rules and standards, these rules must actually be put into practice and accountants and users should have the chance to study and understand them. Finally, there should be a system for monitoring the level of adherence [to the new rules]. And, all of this together presents a task on a considerably larger scale. At the same time, I don't agree with the claim that the first stage of reforms didn't bring any results. First of all, a number of fundamentally new concepts

were borrowed from IAS and introduced into Russian Accounting Rules. For instance, such concepts as «related parties», «goodwill», «segment information» and «contingent liabilities». Secondly, Russia won recognition among the international professional community, and a representative from Russia now sits on the LFRSC. Third, the Institute of Professional Accountants of Russia was founded, and become a member of International Federation of Accountants and it's difficult to overestimate the positive role that this professional association has played in transforming the field of accounting. Fourth, more and more companies are intentionally switching over to IAS. Before 1998 switching over to IAS was merely a way of showing that a company was up with the latest business trends, it was just a symbol of success – like buying the latest model Mercedes. Fifth, Russian universities have started to include IAS as a separate discipline in their curriculum. Wouldn't you call these real results? But, for sure, one always wants to achieve more.

***What are the conceptual differences between IAS and Russian Accounting Rules (RAR)?***

RAR represent a system of instructions on specific issues, whereas IAS merely set the requirements and principles for financial reporting, which individual accountants must implement using their own professional judgment. Under IAS, economic substance prevails over form. The substance of a transaction is what's important, not the type of contract it was carried out under. Take, for instance, a lease agreement. If it is drawn up so that all relevant risks and benefits remain with the lessee, then according to IAS the subject of the lease will be recorded in the latter's reports (although the lessor retains the right of ownership as before).

There are also differences concerning the volume of disclosed in-

formation. Although significant steps forward have been made in Russian Accounting Rules, given that they now require disclosure of a volume of information that simply would have been impossible to imagine just a few years ago. Nonetheless, it is still not quite the volume that is required under IAS.

***But, don't you think that the forced introduction of IAS will only give rise to new problems?***

The transition to IAS is a worldwide trend. Sticking to old standards simply means that one is swimming against the current. If Russia has resolved to build a Western-type economy, then it should strive to conform to the standards of such an economic model. And, that includes accounting practices.

I'm confident that it won't take Russia long to «catch up» with the West and that the country will soon emerge as a strong player. However, this will happen only if Russian accountants are diligent students. At the turn of the 19<sup>th</sup> and 20<sup>th</sup> centuries, the Russian school of accounting was one of the world's strongest. This gives us reason to expect that, instead of being an outsider, Russia is capable of becoming a leader in this field.

Internal Russia-specific factors aside, there are also external factors that hinder Russia's transition to IAS. Take, for instance, the unresolved issue of whether IAS should be recognized on an equal footing with US GAAP in international capital markets...

The less-than-complete recognition of IAS in the United States is no reason to justify a go-slow approach to adopting IAS in Russia. The differences between IAS and US GAAP cannot possibly be compared with the differences between Russian Accounting Rules and IAS. In the first case, the distinction lies in particular issues, rather than in fundamental principles and concepts. This allows for a relatively easy transition from IAS accounts to US GAAP accounts. But, transitioning from Russian account-

ing reports into IAS accounts is a significantly more complex process. Besides, a whole series of special measures are now being taken to secure the recognition of IAS in the US market. And, we can already see definite progress in this area.

***Will the transition to IAS encourage an influx of investment?***

Yes and no. It will, because investors will be able to receive information that will help them to assess the object of a potential investment. Consequently, investment risks will go down, while trust in Russian management will grow. But, on the other hand, it will not, since accounting is not the sole issue here. Yes, the quality of a company's financial statements tends to attract investment, but is not the crucial factor. The transition to IAS will not bring any downpour of golden rain in its wake. There are things that are more important for creating a favorable investment climate.

***How will Russian companies benefit from switching to IAS?***

This is probably the most complicated question of all. At first glance, it appears that IAS will primarily facilitate a company's entry into global financial markets. Nevertheless, most Russian enterprises are anticipating quite another benefit. The application of IAS gives managers access to information that can be used to significantly enhance management effectiveness, and enables them to have a knowledgeable dialogue with shareholders and the marketplace, as well as enhance corporate transparency, strengthen corporate governance, and, consequently, bolster trust in management. Aside from this, using IAS helps to improve the overall business climate in the country and strengthens a businessperson's sense of confidence.

***How can companies adapt IAS with minimum losses?***

First and foremost, companies should not be forced to undergo the transition process overnight. This

would only cause anxiety among accountants and nothing good would come out of it. Secondly, IAS should be adapted to the Russian economic environment. Thirdly, demand for IAS information should be stimulated. The process will become much less painful when managers and Russia's investment community understand the advantages that IAS can bring them. Furthermore, it may be apropos here to recall the once popular in the Soviet Union slogan: one must learn, learn and learn some more. And, we should begin not with the specific rules themselves, but by first studying the fundamental philosophy on which they are based.

Russian accounting may differ from that required by IAS because of the absence of specific Russian rules on recognition and measurement in the following areas:

- the classification of business combinations between acquisitions and unitings of interest: IAS 22.8
- provisions in the context of business combinations accounted for as acquisitions: IAS 22.31
- consolidation of special purpose entities: SIC 12
- the restatement of financial statements of a company reporting in the currency of a hyperinflationary economy in terms of the measuring unit current at the balance sheet date: IAS 29.8
- the translation of the financial statements of hyperinflationary subsidiaries: IAS 21.36
- the treatment of accumulated deferred exchange differences on disposal of a foreign entity: IAS 21.37
- impairment of assets: IAS 36
- derecognition of financial assets: IAS 39.35
- the recognition of operating lease incentives: IAS 17.25; SIC 15
- accounting for defined benefit pension plans and some other types of employee benefits: IAS 19.52

- accounting for deferred tax: IAS 12
- accounting for an issuer's financial instruments: IAS 32.18/23
- hedge accounting for derivatives: IAS 39.142
- the treatment of exchange differences resulting from severe devaluation or depreciation of a currency: IAS 21.21; SIC 11
- recognition of a decline, other than temporary, in the carrying amount of long-term investments, other than marketable equity securities: IAS 25.23

There are no specific rules requiring disclosures of:

- a primary statement of changes in equity: IAS 1.7
- a primary statement of cash flows; and the notion and definition of cash equivalents, and detailed guidance on the preparation of cash flow statements: IAS 7
- the FIFO or current cost of inventories valued on the LIFO basis: IAS 2.36
- the fair values of financial assets and liabilities: IAS 32.77
- the fair values of investment properties: IAS 40.69
- related parties information except by certain reporting companies with specific legal form (joint stock companies); the definition of a related party is a narrower one, based on legislation: IAS 24.1-4
- discontinuing operations: IAS 35
- certain segment information (e.g. a reconciliation between the information by reportable segment and the aggregated information in financial statements, significant non-cash expenses, other than depreciation and amortization, that were included in segment expense and, therefore, deducted in measuring segment result – for each reportable segment): IAS 14.61/67

There are inconsistencies between Russian and IAS rules that could lead to differences for many enterprises in certain areas. Under Russian rules:

- research costs can be capitalized under certain conditions: IAS 38.42/51
- goodwill is calculated by reference to the book values of acquired net assets: IAS 22.40
- proportionate consolidation may be used for subsidiaries in which the parent has 50 per cent or less of the voting power: IAS 27.15
- revaluation of property, plant and equipment is allowed but gives different results than IAS and need not be kept up-to-date: IAS 16.29
- the useful life of property, plant and equipment is usually determined using periods prescribed by government for tax purposes which are longer than those for which the assets are expected to be used: IAS 16.6/41
- if investment properties are revalued, they are still depreciated: IAS 40.27
- if investment properties are revalued, the gains and losses are not required to be taken to the income statement: IAS 40.28
- finance leases are generally defined in legal terms and capitalization is allowed but not required: IAS 17.3/12.28
- lessors recognize finance lease income differently: IAS 17.30
- the completed contract method can be used for the recognition of revenues on construction contracts when the outcome of a construction contract can be estimated reliably: IAS 11.22
- trading, available-for-sale and derivative financial assets are not recognized at fair value: IAS 39.69
- trading and derivative liabilities are not recognized at fair value: IAS 39.93
- provisions can be established more widely or less widely than under IAS, and there is no requirement for discounting: IAS 37.14/45
- own (treasury) shares are shown as assets: SIC 16
- classification of cash flows between investing and financing activities in the cash flow state-

ment may be different from IAS: IAS 7.6/16/17

- cash flow statements reconcile to cash rather than to cash and cash equivalents: IAS 7.45
- the correction of fundamental errors is included in the determination of the net profit or loss for the reporting period, but separate disclosure and pro-forma restated comparative information are not required: IAS 8.34/38
- revenue recognition rules do not differentiate between exchanges of goods of similar nature and value and exchanges of dissimilar goods, and do not discuss adjustment for the amount of cash or cash equivalents transferred in exchanges for dissimilar goods: IAS 18.12; IAS 16.21/22
- the definition of extraordinary items is broader: IAS 8.6/12

In certain enterprises, these other issues could lead to differences from IAS:

- some parent companies do not prepare consolidated financial statements: IAS 27.7/11
- in the definition of control, the ability to govern decision-making is not required to be accompanied by the objective of obtaining benefits from the entity's activities: IAS 27.6
- investments in certain securities held for the short term are not required to be carried at the lower of cost and market value or at market value: IAS 25.19/23
- certain subsidiaries may be excluded from consolidation beyond those referred to in IAS: IAS 27.13
- a subsidiary that is a bank may be excluded from consolidation if it is dissimilar from the rest of the group: IAS 27.14
- certain set-up costs that have been paid by a company's founder can be capitalized: IAS 38.57
- internally generated brands and similar items can be capitalized if the enterprise has an

exclusive legal right: IAS 38.51

- inventories are generally carried at cost rather than at the lower of cost and net realizable value; this is often not an important difference because of inflation: IAS 2.6
- the realizable value of inventories can be measured without deduction of selling costs: IAS 2.6
- certain overheads in addition to those related to production can be capitalized: IAS 2.7

*Leonid Schneidman, Partner of PricewaterhouseCoopers and Head of the Audit and Accounting Methodology Department. This interview has been reprinted from the RBCC Bulletin (№2, 2002) with the permission of PricewaterhouseCoopers.*

## FRC meeting with FCSM

**T**he next FRC meeting took place on 17 May 2002 and was supported by the FCSM of Russia. The discussions at the meeting involved the following topics: recommendations to the IASB Board on introducing changes to the standards regulating issues on accounting and reporting of financial instruments, and also practical problems the Russian companies are facing when applying IFRS in regard to financial instruments accounting.

During the discussion the participants agreed not to assess the recommendations of the IASB Board on making changes to IFRS 32 and 39 until the Exposure Draft of the corresponding standard is published (according to the schedule of the Board this document is expected to be published during the second quarter of the year 2002). The Council is planning to get back to the discussion of the recommendations during the period opened for comments on the Exposure

Draft. The discussion of certain issues regarding the practical application of IFRS 32 and 39 has proved the necessity for further consideration of evaluation of financial instruments in the absence of active market environment for such instruments, and also other issues that would involve certain specialists from audit firms and other companies providing IFRS reporting.

The meeting was also focused on the evaluation issue of initial recognition of interest-free loans made by the company, and also borrowings and loans issued at a lower than the market rate (IAS 39 Implementation Guidance, Question 66-3). It was agreed to present the position of the Council on this matter to the IASC Board and the Recommendation Committee on the IFRS 39 application.

In the context of the meeting the discussion took place on the development of a plan for a short-term perspective for the working group at the FCSM of Russia on IFRS implementation. The enforcement of IFRS in Russia is considered a priority issue for the working group aimed at regulating the process of preparing and presenting the financial reporting in compliance with IFRS.

The Council has also approved the procedure that the working group should follow to make an expert evaluation of the Russian translation of IFRS to equip Russian companies with a unified set of tools needed by the Russian speaking users for presenting financial statements in comprehensible and compatible terms.

The Provisional Regulation on the working group of financial reporting in the extractive industries was also approved. Yegor Metelkin, senior manager of the audit department, Deloitte & Touche, was appointed Chairman of the working group.

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## OECD White Paper on Corporate Governance in Russia

*Fianna Jesover*

**A** series of recommendations for improving corporate governance in Russia, drawn up in three years of consultations and debate involving Russian and international policy-makers and businessmen, were recently released by the OECD in Moscow to an audience of policy-makers, business leaders and the press. They were also presented in Paris to high level officials from OECD capitals. The recommendations are contained in a **White Paper on Corporate Governance in Russia** developed by the Russian Corporate Governance Roundtable. Sponsored by the OECD and the World Bank, the Roundtable has brought together an influential network of Russian and international policy-makers and private-sector decision-makers in five meetings over the last three years. The White Paper, whose text has been the subject of extensive open consultation, is expected to contribute to reform and policy-making in Russia over the coming years.

Until recently, poor corporate governance practices have impeded the development of a sound investment climate in Russia. Much progress has been achieved, however, during the last few years. Laws have been adopted or amended to strengthen protection against abuses. Policymakers, investors and the public at large have become aware of the issues and have pressed for change. Some

of the largest corporations, previously the source of notorious abuses, appear to be changing their practices for the better.

This progress has been fully recognised and acknowledged by the Roundtable. The credibility of corporate governance and the development of equity markets in Russia now depend on sustaining the momentum of these reforms, deepening their impact and rendering them enforceable and irreversible. To achieve those goals, priority should be given to the following five areas:

### **1. Intensify implementation and enforcement**

The highest priority is to strengthen the legal and regulatory framework to ensure that existing laws and regulations are implemented and enforced effectively. This is needed for the proper functioning of companies as well as securities markets. Effective implementation requires both sustained levels of investigation and enforcement as well as credible sanctions — severe enough to deter violations. Of particular importance to enforcement are provisions for the equitable treatment of shareholders, expropriation of corporate assets by managers or controlling shareholders, and violations of disclosure requirements.

The legislature and the government should strengthen the judiciary's ability to deal with commercial disputes. Courts need more resources to hire, retain and train judges and other staff so they can perform their functions in a fully professional manner and with the required level of integrity. Streamlining the rules on jurisdiction over commercial disputes will result in a coherent, predictable body of precedent and also help in developing the necessary body of expertise among judges.

The Federal Commission for the Securities Markets (FCSM) should be granted sufficient resources to pursue its core func-

tion: to develop and enforce regulations that protect inventors and maintain market integrity. The mandate of the FCSM should focus explicitly on the supervision of market intermediaries and the monitoring of publicly held corporations, in order to make the best possible use of scarce human and financial resources.

Since implementation and enforcement also concern investors and individual corporations, stock exchanges, business associations, professional organisations and individual companies, they should themselves develop and carry out their own strategies for improved corporate governance.

Russia should adopt in full and as quickly as possible International Financial Reporting Standards for publicly listed and non-private companies (widely held non-listed companies). These companies should be audited in compliance with International Standards of Auditing.

### **2. Ensure clarity and coherence**

Priority also should be given to clarifying the competencies of various institutions and ensuring coherence among different legal and regulatory provisions.

Clear responsibility should be assigned to the proper authority for reporting changes in corporate ownership and control. The regulatory authority for supervising the share registrars needs to be clearly specified. The status and liability of senior managers should be clarified and distinguished from those of other employees as set out in labour law. Board members need to perceive their duties and liabilities clearly and explicitly.

### **3. Facilitate the development of a culture of corporate governance in the private sector**

Several Russian companies are beginning to capitalise on the benefits of good corporate governance. To assist them in this proc-

ess, it is important that the legal and regulatory framework is understandable and does not burden corporations with undue administrative costs. It is important to develop and implement regulations that strike the right balance between these costs and their benefits.

It is also important that the corporate sector develops and takes prime responsibility for a set of corporate governance tools, such as a Code of Corporate Governance. Professional associations also need to develop their own ethical and professional standards that ensure legitimacy, better member services, and credibility with market participants and the public at large.

### **4. Ensure continuing support and review of progress**

The reform of corporate governance in Russia is now at a critical stage. To ensure domestic and international credibility, the Roundtable should continue its work using this White Paper as the basis for promoting, assisting and assessing progress in Russian corporate governance. A core group will be formed to guide the work and offer help, advice or expertise on specific issues and related areas of corporate affairs affecting corporate governance such as insolvency. The White Paper should also serve as a resource for Russian authorities and corporations that want to report on progress, seek the opinion of the international business community and identify areas where technical assistance may be required.

### **5. Support and enhance the development of training programmes**

An important task for governmental bodies, professional associations and individual companies is to ensure the effective training of judges, government officials as well as managers, board members, accountants and auditors.

This is particularly important in order to raise the general awareness of good corporate governance, keep up with any changes in the laws, facilitate the transition to international financial reporting standards, and develop professional boards.

To accomplish this task, the Russian government, professional organisations, individual companies and the international donor community need to make available sufficient funds and resources. It is important that the training is adapted to the Russian context and to the needs of practitioners.

In developing these recommendations, the Roundtable has used the OECD Principles of Corporate Governance as a point of reference. The OECD Principles are one of the 12 core standards adopted by the International Financial Stability Forum to promote financial market stability and reduce the risk of future financial turmoil. This White Paper thus establishes a direct link between today's Russian corporate governance agenda and internationally recognised standards.

Broad international participation has been strongly encouraged to ensure full Russian access to today's international dialogue on corporate governance and to give Russian authorities, corporations and investors the opportunity to discuss developments with their peers from OECD countries. The Roundtable, which has taken an inclusive approach to its work, circulated drafts of the recommendations and made them available for comment. The final White Paper incorporated comments to the draft and others made at presentations during the Roundtable meetings.

This White Paper has been developed on a consensual basis. The Roundtable meetings, organised by the OECD in co-operation with the World Bank Group, have been co-hosted by the FCSM and the Supreme Arbitrazh Court. The

Roundtable has also received financial support from the United States Agency for International Development and the Global Corporate Governance Forum.

Participants to the Roundtable have been senior Russian and international policy makers, regulators and market participants. They have included representatives from the legislature, the government, the judiciary, regulatory authorities, stock exchanges, corporations, investors, stakeholder groups and individual experts. Representatives from international organisations, non-governmental groups and bilateral agencies with interest and expertise in corporate governance also participated.

Building on internationally recognised standards, it reflects what is commonly expected from Russian policy makers and the business community in an increasingly global economy. While priorities and details of legislation may differ from country to country, a global consensus on a framework for good corporate governance is rapidly emerging. Regional corporate governance White Papers currently are being developed by similar Roundtables in Asia, Latin America, and South-Eastern Europe.

The recommendations in this White Paper should be viewed as complementing other corporate governance initiatives by private and public institutions in Russia, such as the Corporate Governance Code developed by the FCSM. These recommendations are primarily concerned with corporate governance in publicly traded companies. Improving corporate governance is, however, a shared responsibility between the public and private sectors where individual corporations, investors and professional organisations must play a proactive role. Experience has shown that it is ultimately a matter of self-interest for all members of the business community to evaluate their systems

of corporate governance and implement the recommendations in this White Paper.

The recommendations in this White Paper should also be supplemented by reforms to public governance and corporate governance in the financial sector. Special attention should also be given to corporate governance in the continuing process of restructuring the Russian natural monopolies.

Signs of increased awareness are numerous and encouraging. President Putin has spoken out on the role of corporate governance in fostering a favorable investment climate. The FCSM has coordinated an intensive effort to produce a corporate governance code. The Duma has set up a working group on corporate governance. New private non-profit institutions, including managers and investors associations, investor relations groups, institutes on corporate governance and directors, have been created. Ratings agencies have initiated corporate governance ratings for Russian companies. Most tellingly, many major companies have realized and are taking steps to enjoy the benefits improved governance practices can bring to attract outside investors and to raise their market value.

In the mind of the market, however, once bitten, twice shy. Investors well remember the corporate governance abuses of prior years. It is therefore imperative that Russia maintains the momentum of reform and put in place credible enforcement mechanisms. The need for tangible and irreversible progress requires us to move forward from awareness raising to implementation and enforcement. Essential aspects of this movement will be peer discussion based on real-world experience, the type of discussion which the Roundtable is well-positioned to carry out through its existing constituency and the OECD's network

of experts in the delegations and capitals.

The coalition of Russian and international experts has therefore committed itself to continue the work of the Roundtable, using the White Paper and other relevant initiatives as the basis for promoting and assessing implementation of reform. The continuity of the Roundtable's involvement will preserve a common framework for corporate governance reform and sustain coherence. It will also create synergies among the different group of actors and serve as a nexus for dissemination of new initiatives.

The second phase of the Russian Roundtable's work over the next three years will therefore focus on designing and implementing corporate governance reforms. The main points of reference will be the recently issued White Paper of Corporate Governance and other relevant Russian reform initiatives. Focus will be on identifying viable and effective solutions through an exchange of experiences among public and as well as private sector experts in Russia and their counterparts from OECD member countries and international organisations. The Roundtable will also provide a link between corporate governance reform and related corporate affairs issues, such as insolvency reform, and help identify areas where technical assistance may be required. The OECD remains a trustworthy and committed partner in helping to drive the work of the Roundtable forward.

*For further information, on the White Paper contact Fianna Jesover, Project Manager at the OECD's Corporate Affairs Division (tel: [33] 1-49-10-4345 or e-mail: [Fianna.JESOVER@oecd.org](mailto:Fianna.JESOVER@oecd.org)). For information on all the work the OECD undertakes in Russia contact Nick Malyshev at the OECD's Centre for Co-operation with non-members (tel. [33] 1-45-24-1669).*

## Accounting Reform

**T**he issue of accounting reform remains outstanding and in urgent need of resolution.

Russian statutory financial statements (which retain many aspects of the financial reporting system of the socialist era) are unsuitable for use in effective decision-making, and are inconsistent with generally accepted standards on the disclosure of information in a market economy. The lack of transparency throughout the economy as a whole, and within individual enterprises, is deterring investment into the manufacturing sector, preventing Russian businesses from entering international capital markets, hampering the development of the financial system, and ultimately, impeding economic growth.

Specifically, it is not possible for banks to establish fully-fledged correspondent relationships with foreign banks without submitting financial statements prepared in accordance with one of the officially recognized international sets of standards [International Accounting Standards (IAS) or US Generally Accepted Accounting Principles (US GAAP)]. Moreover, business entities are being prevented from raising financing on the capital markets by the weaknesses inherent in, and potential inaccuracy of, their Russian statutory financial statements.

Furthermore, the process of globalization makes it increasingly important for all countries involved in economic integration to apply a uniform set of principles to financial reporting. International Accounting Standards (IAS) has received

official recognition as the future global standard on the disclosure of financial information from the major multinational corporations. The US Securities & Exchange Commission (SEC), which is playing a direct role in the reorganization of the International Accounting Standards Committee (IASC), has come out clearly in favor of the amalgamation of the two accounting systems: US GAAP and IAS. The International Organization of Securities Commissions (IOSCO) has issued a resolution recommending that the application of IAS should be made a condition for companies to be listed on international securities exchanges, and has already taken a number of tangible steps in that direction.

However, the two-year accounting reform program that was launched in Russia in 1998 has not been completed. Less than 20 out of the required 37 standards have been drafted. This slow progress is a result of the poor level of commitment on the part of the parties to the project<sup>1</sup>. The decisive role in the development and adoption of accounting standards continues to be played by an inter-agency Government Commission in which the Ministry of Finance holds a key position, but which lacks any representation of the business community. Private sector specialists are engaged, at best, in the role of advisors, and have no right to vote in the commission.

<sup>1</sup> State agencies, above all, the Ministry of Finance, believe that Russian Accounting Standards are being developed in accordance with IAS and that the key task is to ensure their phased implementation. Auditing and advisory firms face a significant demand for their services fueled by the existence of two different sets of standards and the need of translating financial statements from one format to the other. Businesses, primarily those companies which have to maintain their accounting records under both domestic and international standards, are the only community which is effectively interested in reducing the timeframe for IAS transition. In other words, the most competitive Russian entities which are of interest for investors and are creditworthy incur double expenditures to compile their financial statements.

This gradual replacement of standards is not the correct approach. It increases the operating costs incurred by businesses and statutory bodies, and distorts the accuracy of reported data<sup>2</sup>. The proper approach would be to immediately implement the entire set of international accounting standards and then draft regulatory instruments and recommendations to allow for specific aspects of the Russian economic environment.

The ongoing development of information technologies<sup>3</sup> and the increasingly advanced qualifications and experience of financial staff at companies operating in Russia, who have coped admirably with the problems brought about by the constant changes to the tax legislation, indicate that accounting reform is something that can be carried out relatively quickly.

*The key to reforming the financial reporting system involves drafting a legislative framework that is consistent with the rest of the legislation, complete, transparent, and coherent. This is a task for specialists and does not require substantial capital investment, institutional reorganization, or favorable exogenic circumstances, etc. The speed with which accounting reform is carried out is in many ways determined by the level of Government commitment and the insistency of the business community.*

*This material has been reprinted from the «Investment Climate in Russia» report prepared by Ernst & Young and Expert Institute.*

<sup>2</sup> In particular, according to effective Russian Accounting Statutes (PBUs), there is a group of «low-value and short-life items» which is absent in IAS. Also, they are based on different principles of asset valuation, depreciation and impairment, and the problem of high inflation (as well as hyperinflation) is ignored.

<sup>3</sup> For example, at present Konsultant Plus delivers CD-ROMs with updated legislation to approximately 100,000 offices weekly. Many companies now have sufficient financial resources to secure the delivery of new legislation to all need-to-know users within two weeks.

## IFAC News

### IPA joins IFAC

At its' meeting in November, the IFAC Board agreed to admit three new bodies to full membership: National Chamber of Statutory Auditors of Poland, Institute of Professional Accountants of Russia, and the Slovak Chamber of Auditors. IFAC members now comprise 156 professional accountancy bodies in 114 countries, representing more than 2.4 million accountants.

### Five New Accounting standards for the Public Sector

IFAC's Public Sector Committee (PSC) has made significant headway in developing international accounting standards for governments and their agencies by releasing five new International Public Sector Accounting Standards (IPSASs) and a new exposure draft. This brings the total of accrual-based standards to 17. PSC anticipates completing development of the remaining three core IPSASs by mid-2002.

The new IPSASs are as follows:

**IPSAS 13 – Leases.** This standard prescribes for both lessees and lessors the appropriate accounting policies and disclosure to apply in relation to finance and operating leases. It includes guidance on the classification of leases, disclosures to be made in the financial statements of lessees and lessors, and accounting for sale and leaseback transactions.

**IPSAS 14 – Events after the Reporting Date.** This standard prescribes when an entity should adjust its financial statements for events which occur after the reporting date and the disclosures that it should make about other «non-adjusting» events which occur after the reporting date.

**IPSAS 15 – Financial Instruments: Disclosure and Presentation.** This standard prescribes how financial instruments are to be classified and identifies disclosures to be made in general purpose financial statements.

**IPSAS 16 – Investment Property.** This standard prescribes requirements for accounting for investment property, including the initial and subsequent measurement and disclosure of such property by governments and their agencies.

**IPSAS 17 – Property, Plant and Equipment.** This standard prescribes requirements for the initial recognition and measurements of property, plant and equipment. It also deals with subsequent measurements, depreciation and disclosures about these assets. The standard provides a transitional period to support the orderly implementation of its requirements and allows, but does not require, heritage assets to be recognized in general purpose financial statements.

### New Audit Guidance on Banking from IFAC

To assist bank auditors IAPC has released two new International Auditing Practice Statements (IAPS): *Audits of the Financial Statements of Banks* and *The Relationship between Banking Supervisors and Banks' External Auditors*.

The new practice statements highlight the tasks, responsibilities, and challenges facing external bank auditors and bank supervisors and consider special reporting relationships between auditors and bank supervisory and other regulatory authorities.

*Audits of the Financial Statements of Banks* (IAPS 1006), issued after consultation with the Basel Committee on Banking Supervision, focuses on the various stages of the audit of a bank

with emphasis on those matters that are either peculiar to or of particular importance in such an audit. Also included are appendices that contain examples of –

- Typical internal control procedures and substantive audit procedures for two of the major operating areas of a bank – lending and treasury operations;
- Financial ratios commonly used in the analysis of a bank's financial condition and performance
- Risks and issues in securities operations, private banking and asset management; and
- Typical warning signs of fraud.

*The Relationship between Banking Supervisors and Banks' External Auditors* (IAPS 1004), which has been developed in conjunction with the Basel Committee, provides information on how the relationship between bank auditors and supervisors can be strengthened to mutual advantage, taking into account the Basel Committee's Core principles for Effective Banking Supervision. Specifically, this IAPS –

- Describes the primary responsibilities of the board of directors and management;
- Examines the essential features of the role of external auditors;
- Examines the essential features of the role of supervisors;
- Reviews the relationship between the supervisor and the auditor; and
- Describes additional ways in which auditors and the auditing profession can contribute to the supervisory process.

### **Auditing Fair Value Accounting**

To address the increasing number of complex accounting pronouncements containing measurement and disclosure provisions based on fair value,

IAPC has developed a proposed International Standards of Auditing (ISA) on fair value measurements and disclosures.

The ED addresses audit considerations relating to the valuation, measurement, presentation and disclosure for material assets, liabilities, and specific components of equity presented or disclosed at fair value in financial statements. The comment period has recently concluded. The US ASB is issuing the IAPC document for public comment and IAPC will be considering comment from both exposure in the development of final guidance which is expected to be issued later this year.

### **New Independence Rules from IFAC**

IFAC has updated its *Code of Ethics for Professional Accountants* to include new rules on independence. The Code states the fundamental principles that should be observed by professional accountants to meet their responsibility to protect the public interest. It includes principles that are applicable to all professional accountants, and distinguishes between those that affect professional accountants in public practice and those that are applicable to other accountants employed in business and industry.

The new rules of independence set out a conceptual framework that focuses on the factors that pose a threat to independence for all assurance engagements and the safeguards that auditors should put in place to preserve their independence. In addition, the updated Code provides examples of situations on how the conceptual approach to independence is to be applied to specific circumstances and relationships. The Code may be downloaded from the IFAC website at <http://www.ifac.org>.

### **The Role of the Chief Financial Officer in the Year 2010 Focus of New International Publication**

Ten chief financial officers from leading companies throughout the world speak out on issues impacting businesses and the role of the CFO in *The Chief Financial Officer in the Year 2010*, a new publication released by the International Federation of Accountants (IFAC). The publication features interviews conducted by Robert Bruce, accountancy editor of The Times, London, with CFOs from North and South America, Europe, and Asia. The CFOs represent diverse fields including telecommunications, electronics, retail, financial services, industrial gases, and consumer products and provide candid comments on what lies ahead for their profession and the businesses they serve.

«The CFOs consistently cited the interpretation and delivery of complex information as the greatest challenges facing them and their employers both today and in the future and see these challenges as shaping the future role of the CFO», points out Bill Connell, director of Risk Management for the BOC Group and chairman of IFAC's Financial and Management Accounting Committee (FMAC).

«As a result of the demands placed on companies by shareholders, regulators and the public at large for increasing financial information, the CFO's role is shifting dramatically from one of transaction manager to communicator and strategist», adds Mr Connell.

Other areas in which the CFOs see their roles expanding include the following:

- Investor relations and reputation management
- Risk management

- Corporate governance
- Global marketing
- Remuneration policies, especially for senior management
- Treasury functions

The interviewees also stressed that as the stewards of corporate financial information, CFOs will increasingly become the «guardians of the corporate conscience».

### **New International Guidance Helps Auditors Address E-Commerce Risks**

Increasing use of the Internet for business-to-consumer, business-to-business, business-to-government and business-to-employee e-commerce is introducing new elements of risk that need to be considered by accountants when planning and performing the audit of financial statements. To assist auditors in identifying and assessing these risks, the International Federation of Accountants (IFAC's) International Auditing Practices Committee (now International Auditing and Assurance Standards Board – IAASB) has issued a new practice statement, *Electronic Commerce – Effect on the Audit of Financial Statements*.

«Growth of Internet activity without due attention by the entity to those risks may affect the auditor's assessments of those risks», points out Dietz Mertin, IAASB Chairman. «For example, an entity's e-commerce strategy may affect the security of the financial records and the completeness and reliability of the financial information produced».

This new International Auditing Practice Statement (IAPS) helps auditors address e-commerce issues by focusing on the following:

- The level of skills and knowledge required to understand the effect of e-commerce on the audit;
- The extent of knowledge the auditor should have about the entity's business environment, activities and industries;
- Business, legal, regulatory and other risks faced by entities engaged in e-commerce activities;
- Internal control considerations, such as an entity's security infrastructure and transaction integrity; and
- The effect of electronic records on audit evidence.

The guidance in this statement is particularly relevant to the application of three International Standards on Auditing (ISAs): ISA 300, *Planning*, ISA 310, *Knowledge of the Business* and ISA 400, *Risk Assessments and Internal Controls*.

«While this statement has been written for situations where an organization engages in commercial activity over a public network such as the Internet, much of the guidance it contains can also be applied when the entity uses a private network,» states Mr. Mertin. «Similarly, while much of the guidance will be helpful to accountants engaged in auditing entities organized primarily for e-commerce activities (often called «dot.coms»), it is not intended to deal with all audit issues that would be addressed in the audit of such entities.»

*Electronic Commerce – Effect on the Audit of Financial Statements* may be downloaded from the IFAC website <http://www.ifac.org/store> for a fee of US\$22; print copies may be purchased for US\$25 plus shipping by calling 1-212-286-9344 or placing an order through the online bookstore.

## **Focus Anti-Money Laundering Issues in the Wake of 9/11**

Barry Eden

**T**he terrorist attacks of September 11, 2001, shocked the world and started a new round of anti-money laundering (AML) regulation initiatives, as national governments sought to adjust their controls of financial systems to enable them to filter out money transfers by terrorist groups. While Russian companies and banks are hardly sponsoring terrorists, Russia's financial system is used, many believe, to launder large amounts of money generated by bribery, drug cartels, and illegal international arms trading. Accordingly, Russia is on the Financial Task Force on Money Laundering's (FATF) blacklist of countries that have not taken adequate measures to prevent money laundering.

As American, British, and Western European financial institutions see their compliance cost soaring, they are sure to shift some of the burden onto their correspondent Russian banks. For this reason, it is now becoming essential for Russian banks and corporate treasuries to understand how international anti-money laundering regulations work and how they are going to impact business as early as spring 2002.

*Money-laundering* is defined as processing the proceeds of criminal activities to disguise their origins. It is used to legalize cash from illegal arms sales, smuggling, and organized crime

activities such as drug trafficking and prostitution rings, as well as embezzlement, insider trading, bribery, and computer fraud schemes. The volume of money laundering transactions performed worldwide each year is estimated by the IMF to be anywhere between \$600 billion and \$1.5 trillion.

This is between two and five times Russia's GDP.

Long before the September 11 attacks, banks were already facing the intensified regulatory scrutiny of their anti-money laundering activities. Now they have been conscripted into the war against terrorism in a major way, as regulators and law enforcement officials seek their assistance in identifying and freezing the assets of terrorists. Let's review some of the new legislation initiatives that will significantly impact Russia's banks doing business abroad.

### ***The FATF and others***

FATF, an AML country group sponsored by the OECD, has also issued a set of eight recommendations in response to the September 11 attacks. These are in addition to its forty recommendations issued previously, which suggest how a «cooperative» jurisdiction should behave.

Some of the FATF recommendations are general, saying that the financing of terrorism should be criminalized everywhere in the world, suggesting that all countries should join a 1999 UN Convention for the Suppression of Financing of Terrorism, and calling for international cooperation.

Other recommendations are quite specific, including the freezing and confiscation of terrorist assets, the requirement to report suspicious transactions, and the requirement to ensure that non-profit organizations are not misused by terrorist organizations. Another potentially costly requirement would compel

information about a person or entity originating a wire transfer to remain with the transfer through the payment chain.

Recent global anti-terrorist activity has prompted the adoption of new anti-terrorist and AML legislation in many countries around the world. More than a dozen countries have announced the drafting or adoption of AML laws over the past five months. Some of the countries that adopted laws (Dominica, the Philippines, and Hungary, for example), or drafted them (such as Indonesia and Egypt) are on the FATF blacklist of non-cooperating countries and needed to adopt and implement these laws to be removed from the list. Other countries that are not blacklisted by the FATF (including the United Arab Emirates, Hong Kong, Ukraine, and Oman) have also said they plan changes in their legislation relating to AML procedures.

Russia adopted AML legislation last year: the Russian AML law was enacted on February 1, 2002. The new law broadly corresponds to the FATF recommendations, even if some provisions appear ambiguous. Russia, however, was not removed from the blacklist during the February meeting of the FATF. Russian officials say that this is primarily because the committee would like to see how the law works in practice before making any decisions. Furthermore, the Russian AML law was adopted before the new Anti-Terrorist Money recommendations were issued. Nevertheless, Russian authorities hope that the country will be removed from the list in the summer of 2002.

### ***What does it Mean for Business?***

It is already clear that Western banks will incur significant incremental costs in accumulating information on people who use their services and in taking ac-

tion against a growing list of unwanted organizations and individuals. Substantial effort is involved in screening true hits from false ones because the lists involve numerous aliases and possible stolen identities. Moreover, account activity must be reviewed for any hits going back five years, and law enforcement officials are not yet able to advise banks on what they should do when they have a hit.

Non-banking financial institutions such as insurers, asset managers, and investment banks, which have never before been required to monitor accounts for suspicious activity, may now be required to do so. The new US anti-terrorism legislation defines «financial institution» very broadly, meaning that insurers, securities brokers/dealers and asset managers will be required at least to enhance their anti-money laundering programs and related internal audit activities.

It is inevitable that Western banks and non-banking organizations will share their new compliance burden with their foreign correspondent banks. In fact, the U.S. anti-terrorism law requires that any foreign bank with an account (but without a facility) in the U.S. will have to designate an agent for the service. That opens the foreign bank up to substantial new liabilities and increased costs. Moreover, the U.S. can at some stage freeze an account of a foreign bank simply because it has not yet frozen certain «terrorist» accounts in a home country.

All Russian banks may be affected by the various special measures the U.S. Treasury may impose on relationships with problem foreign jurisdictions and/or institutions. And apparently Russia may be considered as a problem jurisdiction at least as long as it stays on the FATF blacklist. Taken together, this means that Russian entities that

have correspondent accounts or that do business with American, British and other Western financial institutions should be prepared to comply with the laws of the jurisdictions in question.

Russian companies outside the financial services sector will be less directly impacted. Nevertheless, given that many of them have quite a complicated «group» structure spanning to several international jurisdictions, corporate CFOs may also have to initiate an extensive review of the structure to minimize the risk of having their payments disrupted or overseas assets frozen because of suspicious transactions.

*Barry Eden is Partner in charge of financial services, Ernst and Young Moscow office. This article has been condensed and reprinted from the Business Perspective (March–April 2002).*

## European News

### Germany Issues its Corporate Governance Code

In March 2002 a German government-appointed commission produced a code of corporate governance. By law, all quoted companies will have to say whether they comply with certain of its recommendations or explain how and why not. The code is too weak for some critics: companies will not have to disclose individual directors' pay, for instance. Yet it does attempt to improve Germany's two-tier board system—in particular, by making supervisory boards better guardians of shareholders' interests, despite the presence on these boards of workers' representatives and ex-managers.

## FEE Addresses the Role of Accounting and Auditing in Europe

***Recent high profile international business failures have seen concerns raised regarding the current state of corporate governance and financial reporting in Europe. With its new position paper FEE<sup>1</sup> is highlighting the essential issues for the accountancy profession at the center of the current debate.***

Financial statements presenting a true and fair view of a company's financial position are a cornerstone of any capital market. A major listed company's unexpected collapse risks undermining the credibility of the financial information presented to the market place, and the regulatory system which is put in place to protect investors.

FEE, as the representative organisation of the accountancy profession in Europe, understands the seriousness of the questions raised by recent events. Also, we recognise the fundamental importance of public trust in our profession and the need to work continuously to maintain that trust.

The key areas in the debate concern: financial reporting standards; enforcement of standards and corporate governance; auditing standards and quality assurance; ethical standards and independence; oversight of the profession; and auditor liability (protection from catastrophic loss disproportionate to auditor responsibility).

FEE has issued a new policy paper that focuses on the accounting and auditing professions' commitment to high quality financial reporting, all major influences on the quality of financial reporting should be considered, including the role of other professions and regulators.

FEE believes that there is a need to strengthen corporate governance arrangements so that they are equally effective across Europe corporation directors, audit committees and supervisory boards have a key role to play. Others in this debate include enforcement bodies, stock exchange, sponsors, investment bankers, investors, analysts, rating agencies and the financial press.

FEE intends to work with all partners in this debate to maintain momentum and, where necessary, suggest additional initiatives to preserve and enhance the effectiveness of the financial reporting system.

Major steps have already been taken to improve the current financial reporting system in Europe, for example EU adoption of International Financial Reporting Standards (IFRS) and the Commission's recommendation on auditor independence. FEE has played a proactive role, working closely with European Institutions. The paper provides a snapshot of the current situation; outlining the progress made to date and recommending areas that need to be improved. It provides insight into those issues which FEE considers priorities.

FEE strongly believes that recent EU initiatives have strengthened the credibility of the financial reporting system and they are a signal of political commitment to continue to strengthen the quality of European corporate disclosure. The forward-looking strategy adopted by the European Commission, and supported by FEE, should now be given a higher priority.

<sup>1</sup> The Federation des Experts Comptables Europeens (FEE) is the representative organisation for the accountancy profession in Europe. It groups together 38 professional bodies from 26 countries, including all 15 Member States of the European Union and 3 member countries of EFTA. Between them, these bodies have a combined membership of 450,000 individuals, of whom approximately 95% are from EU countries.

FEE believes that action is needed in:

- Ensuring that the European Financial Reporting Advisory Group (EFRAG) makes a significant impact in providing a European contribution to the international financial reporting standard setting process (IFRS and IFRIC);
- Ensuring effective enforcement of IFRS in Europe by 2005;
- Coordinating initiatives in the Member States on the enforcement of financial reporting standards, in order to ensure consistency in application decisions within Europe;
- Agreeing on the FEE proposal to require the application of International Standards on Auditing in Europe by 2005;
- Increasing effort to support and influence the global standard setting process in auditing;
- Speeding up national programs of quality assurance in conformity with the EC's recommendation;
- Stimulating the implementation of the European Commission's recommendations on statutory auditor independence;
- Improving the current situation in the area of auditors' liability; and
- Defining at EU level harmonised conditions for organising the public oversight of the auditing profession in the EU Member States.

Commenting on the current debate, FEE President Goran Tidstrom said:

«The accountancy profession has made substantial efforts over many years to provide business and capital markets with high quality accounting and auditing standards. As demonstrated by its action in recent years, FEE has been proactive in its contribution. FEE will continue to work on behalf of the European profession to raise standards and to highlight areas of concern.

*The position paper The Role of Accounting and Auditing in Europe is available free of charge and can be downloaded from the FEE website <http://www.fee.be>.*

## Accounting Reform Is Complex and Ambitious

**Mr. Damant recently published a letter in the «Financial Times»**

**T**he «Financial Times» recently issued a comment the new IASB was somewhat slow in making progress, but in fact it seems the position is more complex as Mr. Damant explains.

Sir, Your leader on the work of International Accounting Standards Board («Small tablets», May 15) does not reflect the true state of affairs. As a member for 14 years of the board of the former International Accounting Standards Committee, representing investment managers, perhaps I could describe the position. The IASB is not guilty of the faults you imply. Rather, the problem is more fundamental and more serious.

The IASB is indeed developing standards based on principles, as you recommend. The principles have been created over the past 80 years and gradually implemented – both by the IASC and by national jurisdiction – but so far this implementation has been partial. The new board will do the job properly – but what does that entail?

There will be a rapid move to fair values in the balance sheet, including, in the due course, fair values for the company's own debt. The income statement will show all changes in shareholders' funds (except for transactions with owners as owners).

Assets and liabilities – already defined – will be included in the balance sheet as defined, thus eliminating many special purpose vehicles (as used by Enron) and abolishing the smoothing of pension fund liabilities – as correctly done in FRS 17. Operating leases will be abolished.

In this context your remark that «patience is not unlimited» is absolutely inappropriate and shows little appreciation of the task in hand. The principles must be most carefully examined and implemented. The work involved is tremendous. Powerful interest groups may not like the conclusions, which must therefore, and in any case, be carefully set out. The complaint is likely to be of haste, not (as you imply) delay.

Full fair-value balance sheets? The abolition of this traditional profit-and-loss account? How many of those involved are ready for this? How many have read the principles or thought about them? For example, many of the comments on FRS 17 – even from important places – do not discuss the principles at all.

Your remark that after a year some may find it «exasperating» that the IASB is so unambitious simply does not reflect reality. The fundamental problem is rather that as the work of the IASB appears over the next 12 and 24 months, only a few will agree or understand, even though the work is entirely in line with what you would recommend in the way of a principled approach.

*David Damant,  
Former Chairman,  
British, European and  
International Analysts'  
Organisations.*

## ENRON – the Next Steps

**R**arely, if ever, have the newspapers carried so much coverage – both in reports and commentary – on accounting issues, both technical and political, than in the immediate aftermath of the Enron case.

Despite the emphasis that has been given to the role of Andersen in the Enron affair, the problems exposed by the largest bankruptcy in US history go much deeper than a possible breakdown in auditor performance. Enron has triggered an enormously wide-ranging debate and has raised questions about many aspects of the operation of capital markets as well as concerns about financial reporting and auditing standards, regulatory arrangements and the quality of the corporate governance in major corporations. This article sets out ACCA's views on each of these issues.

### Capital market regulation

The collapse of Enron occurred in the capital market which is not only the largest in the world but which considers itself to be the best regulated. As a result, all capital markets are in future likely to have to devote more resources to maintaining the integrity of their investor-orientated information. ACCA considers that there should be a mechanism which requires both major corporations and institutional investors to provide the resources needed to ensure that the markets function properly – perhaps via an externally administered levy which confers no influence at the regulatory level.

And it is clear that new solutions must be found to global market problems. These will have to be introduced and controlled at individual national level ACCA argues, however, that local solutions should be based on principles

which are agreed at the global level. National regulators and others will need to be prepared to give up a measure of control over their domestic activities in return for influence over global developments.

### Financial reporting

Although the full facts of the Enron collapse will not emerge for a long time, it is already evident that investors were not properly informed about the significance of off-balance sheet finance arrangements. US accounting rules may well have contributed to this in that they are concerned with the strict legal ownership of investment vehicles rather than with their control. By contrast, International Accounting Standards follow the principle of «substance over form» and their use would have resulted in the details of the special purpose entities being reported in a transparent way.

By specifying precisely where the line is to be drawn, legalistic, rules-based standards encourage those who wish to operate as close to the line as possible, or even to test the limits. They enable the exploitation of loopholes and devalue professional judgment.

Standards and rules which are based on principles are greatly preferable. ACCA strongly supports European Union moves to adopt International Financial Reporting and Auditing Standards in the next few years and believes that accounting standard setters and capital markets worldwide which are not yet committed to these should now address the issue urgently. This will, for example, require the US capital markets to commit to the adoption of international standards in preference to established US GAAP and GAAS.

Where a rules-based approach is used, however, standard setters must act firmly and quickly on controversial subjects. The Enron collapse has called into question the speed of response of

the US financial reporting standard setting body. Lobbying, either direct or through government, by those with vested interests in avoiding change is a danger to all national standard setters. There are some indications that, in the Enron case, active lobbying may have contributed to delays in issuing standards to govern the treatment of the special purpose entities used in off-balance sheet financing transactions.

It is also clear that the inappropriate recognition of revenue remains a major challenge for accounting standard setters. Many of the most celebrated corporate collapses of the last 30 years – from railroads to dot.coms – have their origins in the mis-statement of reported revenues. Standard setters and auditors alike need to focus on the principles of revenue recognition not just when bull markets turn sour but at all times.

### Auditor independence

Enron, and all the other cases which have attracted attention, have demonstrated the need for greater transparency and trust. The global financial community should address this as a matter of urgency. No single measure is likely to deal with the questions which have been raised and a range of ideas must be considered. These could include:

- making the appointment of the external auditors less dependent on the executive directors and involving the non-executive directors, audit committee and institutional shareholders, in turn, this would have far-reaching implications for the corporate governance mechanism;
- limitations on the ability of audit firms to offer consulting services to listed company audit clients (although not necessarily a ban on the provision of such services to non-audit clients)
- fuller disclosure of audit and consulting fees in the annual report and accounts;

- a mandatory review by a company's audit committee of the independent status of the external auditors and the publication of a statement that it is satisfied with the results;
- a prohibition on audit firms providing audit services in instances where audit staff have moved to senior executive roles in client companies – this could take the form of a moratorium prohibiting auditors from moving to audit clients for an appropriate period after they have been personally involved with the audit.

There is also the issue of the size of the audit fee relative to the local office which is providing the service and the fee generation target(s) set for the engagement partner. While this cannot be dealt with by prescriptive regulation, audit monitoring should focus on the culture within audit practices and the pressures on individual engagement partners.

ACCA also believes that the process of audit appointment should be reviewed. Although in theory this is a matter for shareholders, in practice the appointment is controlled by management. It may be time to see if this can be changed. One possibility is that private sector or even governmental bodies might fulfill the role of appointing auditors but for multinational companies a global, not national, approach would be necessary. This approach would require the full backing of regulatory authorities worldwide. An alternative approach would be for non-executive directors and corporate audit committees to have a much higher profile role in the auditor appointment process.

### **Audit monitoring**

Professional bodies must have independent investigation and disciplinary procedures and be seen to act in the public interest. This enables them to take firm and transparent action against members who fail in their fundamental

responsibilities, whether as executives or as auditors.

The UK system of quality control avoids firm-on-firm review and instead utilises, through professional bodies, permanent monitoring staff, who are not connected with individual accounting firms. This sort of system, which can both operate on a national basis and cover transnational audit firms, is demonstrably more effective and independent than the widely used and much criticised system of «peer review».

### **Non-executives and the risk management process**

ACCA believes that the ultimate responsibility for ensuring effective corporate governance – including the implementation of robust internal control and internal audit mechanisms – rests with the Board as a whole. In line with the recommendations of the Turnbull Report, Boards of listed companies should ensure that appropriate mechanisms are in place for identifying and managing risk, and should report publicly on these matters. As independent agents, however, non-executive directors have a particular responsibility to investors to ensure that corporate governance processes are appropriate and effective. We believe that there is a case for reviewing the effectiveness of non-executive directors in fulfilling this responsibility and, if necessary, for providing them with an enhanced role in the communication process.

### **Executive remuneration and sustainable wealth creation**

The concept of payment for performance is widely accepted. When, however, it is applied to the remuneration of senior executives, it may do more than simply encourage good performance. It may also incentivise short-term and self-motivated decisions which are not in the long-term interests of investors.

Investors will be better served if performance-related compensation is linked to the longer term generation of corporate wealth. There is an obvious conflict between, on the one hand, the pressures of increasingly frequent interim reporting and one year service contracts and, on the other, the need to deliver sustainable investor returns. This might be addressed by the introduction of remuneration schemes which reward sustainable year-on-year growth in profitability and shareholder value. The trend towards shorter contractual arrangements may also need to be reviewed.

### **Non-executive directors**

The Enron audit committee has been criticised for failing to control the apparent exploitation of US accounting rules to present a better picture of performance than was the actual case. Consideration needs to be given to the time commitment and effort which is required from non-executive directors whose role is to look after the interests of the investors and other shareholders they are there to represent. They should bring to their role a balance of experience and new thinking, some real understanding of the sector in which a company is operating and the ability to make a strategic contribution. And this requires that they are available for meaningful amounts of time.

The independence of non-executives is another critical issue – much commented on by corporate governance lobby organisations. There are obvious weaknesses in a system where former executive directors can become non-executive directors and so in the position of exercising an accountability function in relation to former colleagues.

The development of mechanisms for monitoring and regulating the operation of audit committees also needs to be considered. Such mechanisms should be independent of auditors, who

are not appropriate parties to examine aspects of corporate behavior, which directly affect their own work. The fuller involvement of investors would add greatly to the credibility attaching to governance mechanisms and ACCA considers that it is necessary for investors, particularly institutional investors, to take an active role in monitoring the activities of audit committees. ACCA believes that what is needed urgently is a code of corporate governance which is capable of global acceptance. Such a code should build on initiatives which have occurred in several jurisdictions-of such initiatives include the OECD Principles of Corporate Governance and the World Bank-driven Global Corporate Governance Forum. We strongly urge the promoters of such initiatives to join forces with market regulators – such as IOSCO – and other global organisations – such as the International Federation of Accountants – to develop and promote compliance with a global governance code.

### **Wider disclosure and accountability**

Despite all that has been written and done in recent years, ACCA believes that there is still considerable room for further development of corporate governance practice and reporting. Indeed, there is a need for investor information beyond the narrow confines of the financial statements. Disclosure of corporate governance performance is increasingly relevant: investors, who are right to demand plain language reporting of matters of significance. ACCA champions the extension of corporate reporting to the **wider** economic, social and environmental aspects of a business; investors and other stakeholders are entitled to know how a business responds to the wide range of risks facing it.

### **Our key suggestions**

In summary, therefore, ACCA suggests that:

- global financial markets need a global set of principles-based financial reporting standards and a global code of corporate governance;
- while the necessary new solutions to global market problems and issues of auditor independence will have to be introduced and controlled at individual national level, they should be based on principles which are agreed and co-ordinated at the global level;
- the objectives of financial reporting practice should be expanded to recognise the growing level of concern arising from the globalisation of business;
- the participants in capital markets – both major corporations and institutional investors – should provide the resources to ensure that the markets function properly through an externally administered levy which confers no influence at the regulatory level;
- auditor independence issues should be revisited and the relationship between a reporting entity and its professional advisers should become more transparent;
- there should be a review of the regimes for monitoring practice in auditing, financial reporting and corporate governance.

Enron should be the catalyst for improvements in a range of areas affecting company reporting and governance.

*The article «Enron – next steps» was published in April's issue of ACCA newspaper Accounting & Business. ACCA Russia Representative Office can be contacted for local queries by telephone: (095) 737 5542 or e-mail: [ilya.yuferev@accaglobal.com](mailto:ilya.yuferev@accaglobal.com).*

## **Tacis supports strategic economic reforms**

### **Tacis FINRUS 9802 Accounting Reform**

The project aims at assisting the Russian Inter Agency Committee on Accounting Reform to carry out Russian accounting reform and to develop national accounting standards in accordance with International Accounting Standards.

The project commenced originally in September 1999 and involves providing technical assistance to the Inter Agency Commission on Accounting Reform, which is chaired by Deputy Prime Minister and Finance Minister Kudrin. It has been extended until July 2002.

The original terms of reference of the project involved primarily assistance in the drafting of ten new accounting standards with the topics selected by the Ministry of Finance, with an additional element regarding requirements of SMEs. Whilst the proposals and recommendations of the project in the form of discussion papers and commentaries have been delivered already and have also been presented in a series of conferences, the Ministry of Finance requires more time to consider the proposals and decide what action is to be taken. A closing conference was held on 29-30 November with the participation of Mr Wright (Head of Delegation of European Commission), Mr Sharonov (Deputy Minister of Economic Development and Trade) and Mr Bakaev (Ministry of Finance) and Mr Van der Plaats (European Commission Directorate General – Internal Market) during which members

from the Ministries of Finance and MEDT were presented with a final version of these materials.

In the last months, the scope of the project has been extended primarily in the area of management accounting. The project will assist the Inter Agency Commission in defining a strategy for the encouragement of good management accounting practice and in establishing whether Russian industry is ready to support this development through the creation of a Russian Institute of Management Accounting. A major conference was organised on 18 December in cooperation with Deputy Minister Mr Sharonov (MEDT) to discuss the issues of upgrading management accounting systems in Russian enterprises.

Finally a key achievement of the project has been the creation of an informal group of specialists from large Russian companies who can debate proposals with government officials and the project team in an informal environment. The group has grown from around 20 at the beginning of 2001 to about 120 at its latest meeting on 29-30 November.

#### **Tacis FINRUS 9901 Reform of Auditing**

The project aims at contributing to a significantly increased credibility of audited financial statements of Russian entities subject to compulsory audit by private sector licensed auditors and auditing companies.

The project web site is up and running in both Russian and English versions. Among the material available are a manual on auditing and a series of forms and instructions on how they are used. This, for the first time in Russia, makes available to the smaller audit firms, the systems and techniques similar to those used by the «Big Five» international audit firms.

#### **Tacis FINRUS 9804 Support to Accounting Reform in the Banking Sector**

The project is assisting the CBRF with implementation plans and procedures for reporting by banks in accordance with international accounting standards. Sixteen priority accounting regulations have been drafted by the project and are in the process of being agreed with the project beneficiary, the Central Bank of the Russian Federation, («CBRF»), and being tested at the project's six pilot banks. The project, originally scheduled to finish at the end of November, has been extended to mid-February.

The scheduled training and technical assistance programmes have been completed. The core IAS training courses have been delivered to in excess of 500 participants from banks and training institutions. A total of 29 training events have been held in Moscow and in eight other regional banking centers in Russia. In addition, approximately 60 workshops and seminars have been held at individual pilot banks or jointly for participants from all pilot banks. These covered the core technical assistance subjects of accounting standards and procedures, internal audit, management information systems and broad automation plans. Further training events and workshops are now planned.

*Major generic outputs from the training and technical assistance programmes are available on the project web site: <http://www.tacis-bankreform.ru>.*

*These include: Internal Audit Manual (Volume One) and its companion Field Guide (Volume Two); An Approach to Financial Management – a comprehensive report that gives banks practical guidance on how to design and implement a management information system; Catalogue of Management Reports – compiled to assist in the collection and presentation of accounting*

*and other data for reports to bank management; A Methodological Guide to I.T. Solutions – a guidance paper for banks to assist them to select the correct I.T. solutions, Training Material from IAS courses and workshops. The methodology adopted in the pilot banks to enable them to produce IAS accounts has been the reclassification and adjustment of accounting data used for reporting in accordance with Russian accounting regulations and requirements. The methodology has been incorporated and described in an IAS Conversion Manual, currently in draft form for review by the CBRF.*

## **RID Forum on Corporate Governance**

**T**he second meeting of the RID Forum on corporate governance issues, organized by the Russian Institute of Directors (RID) was held on April 24, 2002 in the conference hall of Rumiantsevskiy Palace (17/6, Maroseika Street, Moscow) under the slogan: "Board of Directors of a Joint Stock Company: Manager or Watchdog".

The choice of the topic is explained by the following reasons. On the one hand, over the past few years we can observe the increased importance of the work of the Board of Directors, better opportunities for the Board's contribution to the company's value and its successful development. On the other hand, drawbacks of the old approaches have become evident, such as orientation on the increasing number of "independent directors" in the Boards and consideration of the minority shareholders' interests.

### **Main speakers at the Forum included:**

- Alexander Branis, Director of "Prosperity Capital Management" investment company, Board member of OAO "Lenenergo", OAO "Nizhnovenergo", OAO "Rostovenergo", OAO "Kubanenergo".  
"Managers and the Board of Directors: Between Scylla and Charybdis (Russian Energy Experience)".
- Vadim Kleiner, Ph.D. (Economics), Director of Analytical Department of "Hermitage Capital Management", Board member of "Volzhanka" Confectionary, member of Sberbank Supervisory Board.  
"The Increased Role of the Board of Directors - Do Shareholders Win or Managers Lose?"

### **Participants of the Forum included:**

**Belikov Igor Vyacheslavovich** – Director of the Russian Institute of Directors

**Berlin Alexandr Davidovich** - Professor of the Moscow State University, member of the supervisory councils of open joint stock company «Krasny Ochyabr» and open joint stock company «Pervy Moskovski Chasovoy Zavod»

**Branis Alexandr Markovich** - Director of "Prosperity Capital Management" investment company

**Grigorieva Alla Borisovna** – Director of the Corporate Governance Department of OAO "Svyazinvest"

**Golikova Viktoriya Vladimirovna** – a researcher at the Institute of Enterprises and Market Analysis of the Higher School of Economics

**Durnov Vyacheslav Sergeevich** – Board Secretary of OAO "KamAZ"

**Zhdanov Alexey Yurievich** – Deputy General Director of OAO "Mining and Metallurgical Company Norilsk Nickel"

**Zhdanovich Dmitry Vadimovich** – Director of External Economic Relations Department of OAO "Surgutneftegaz"

**Kleiner Vadim Georgievich** - Director of Analytical Department of "Hermitage Capital Management" Company

**Konstantinov Gennady Nikolaevich** – Professor of the Higher School of Economics, Director of the Corporate Governance Center at the Higher School of Economics, World Bank expert on corporate governance

**Kochetygova Julia Vladimirovna** – Director for Corporate Governance Rating and Project Evaluation at "Standard and Poor's" Company

**Masiutin Svyatoslav Anatolievich** – Professor, Chairman of the Board of Safonovo Machine Engineering Plant

**Ostarkov Nikolay Alexandrovich** – Head of Intercorporate Relations Department at the Russian Union of Industrialists and Entrepreneurs

**Sinenko Alexandr Yurievich** – Counselor to the General Director, Head of Expert-Legal Department of OAO "Surgutneftegaz"

**Sklyarov Evgeny Yurievich** – General Director of OAO "Fund Yamal"

**Telegin Alexandr Mikhailovich** – Deputy Director of Personnel Department at MPR

**Fedorov Oleg Romanovich** – Deputy CEO of Investor Protection Association (IPA)

**Chebotarev Mikhail Yurievich** – Chairman of the Board of OAO Moscow Confectionery "Krasny Ochyabr"

### **Trainings of Russian Institute of Directors**

Another training course on "Corporate Director" for a group of corporate directors and specialists of several Russian companies, organized by the Russian Institute of Directors (RID), was held on April 13, 2002 in the "Daev-Plaza" Business Center (Moscow).

The following Russian companies and government bodies participated in the training:

- KamAZ
- Svyazinvest
- Metrostroj

- Sibtyazhmash
- Slavich Company
- Tsaritsyno
- Ministry of Property Relations (MPR official is a member of several boards. He represents the stocks in the ownership of the Russian Federation)
- The city government of Trekhgorniy (the Mayor's Office employee is a member of several boards representing the stocks in the municipal property).

In the trainees' opinion, the course has given them knowledge on acute problems and impulse to start looking for the ways to improve corporate governance in their companies.

### **The main topics of the training "Corporate Director"**

- Reasons for the increased importance of the corporate governance in ensuring the effective development of the company;
- Investors and corporate governance;
- Basic models of corporate control. Corporate governance participants;
- Basic components of the Board's effective work;
- The Board's role in the disclosure of information about the company's activity;
- The Board's role in the development and implementation of the corporate strategy;
- The Board's role in the restructuring of the company's management and risk management systems;
- Financial analysis for Board members

### **Trainees' views and impressions**

A. Grigoryeva, OAO "Svyazinvest" Deputy Director of Corporate Governance Department Board member of four Svyazinvest subsidiaries: "I think the training course on "Corporate Director" is useful both for Board

members and for Directors of joint stock companies' departments whose work is related to corporate governance. Such modules as "Organization of the Board's work", "The Board's role in restructuring and crisis management" and "Financial information in the Board's activity" were of special interest to me.

*V. Durnov, OAO "KamAZ" Board Secretary:* "A new RID training course has given me an opportunity to compare corporate governance practices in OAO "KamAZ" with practices in other joint stock companies both in Russia and abroad. Most of the topics presented at the seminar are very useful, for example, "Organization of the Board's work", the topics on the disclosure of information about the company, on the company's strategy.

It seems that nowadays many directors underestimate the role of the Board of Directors and think that the company's efficiency depends on 2 or 3 top managers. Maybe it used to be so earlier. However, a new corporate governance program provides for enhancement of the Boards' role. I think that all those companies' managers who care about the improvement of their professional level should take this course."

The training course on "Corporate Director" was developed in 2001 by the Russian Institute of Directors, with the support of the Federal Commission for Securities Market (FCSM of Russia), in cooperation with the Center for International Private Enterprise (CIPE), USA, and Schulich Business School (Toronto, Canada). Leading Russian and foreign experts, issuer companies, consulting firms and professional securities market participants have contributed to the development of the training course and its adapting to the Russian reality.

The main idea of the course is to create a system of education for different categories of Board members (both executive and

non-executive) of Russian companies. The main goal is to increase their professional level in organizing the Boards' effective activity by encouraging interaction of different categories of corporate directors, with due account of investors' expectations, the latest organization technologies and experience in this sphere, and by ensuring the growth of the Russian companies' value.

*RID President Kakha Bendukidze. RID Director Igor Belikov. Kitaigorodsky Proezd, house 7, stroenie 3, Moscow, RF. Tel.: (095) 220 4535, 220 4540, Fax: (095) 220 4545, Internet: <http://www.rid.ru>, e-mail: [info@rid.ru](mailto:info@rid.ru).*

## Automation of Business Operations: Evaluating Financial Condition of a Company

*Marina Stupakova*

**W**hich qualities make a person successful? First quality is a person's ability to determine his own weaknesses and define areas for his future development. One will not be able to properly set his objectives and find a balance between the desires and realities without determining the above. Besides, during the process of achieving the objective one should administer the performance and compare his current condition against the initial condition. Obviously, to a large extent the environment and

people that a person has to have business relationships during his life effect one's life.

If you draw an analogy with business operations in the market, the same objectives are also important in these circumstances.

Before developing a plan for business development, one should assess the actual condition of an entity. A manager needs to have an understanding of what is the current stage of his entity and how it differs from other companies representing the same industry. With assistance of the accountant a financial director must consider the risks associated with the excess funds or lack of funds at the entity, and determine the amounts of receivables and payables. This may help to answer many questions, such as appropriateness of application for a loan? What shall be the maximum size of a loan to avoid bankruptcy risk exposure? What are the investment conditions?

### *Internal evaluation of the financial condition*

The most accessible information about a company's business is the income statement and balance sheet of a company, which is presented on a regular basis. However, accounts do not fit the needs of the managerial analysis in its pure sense. For example, it can not be used for trend analysis, since the Russian accounting forms and standards constantly change.

Specialized methods are implemented to help to determine relative indicators of company's business using standard reporting data. Accounting data are reported in the integrated form, which helps even in the volatile economic and regulatory environment to perform a vertical (structural) analysis and horizontal (time)

analysis of financial condition of an entity. In other words, this form enables the user to follow trends of every indicator and identify relations between them.

Integrated standard principle is an underlying principle of the computer systems used for financial analysis. These systems are designed for the automation of diagnostics, evaluation and monitoring of financial and business operations of the company. The Audit Expert financial analysis software has been developed on a commercial basis by the Pro-Invest-IT Company as a way to connect in a general sense accounts into compliance with the International Financial Reporting Standards (IFRS). There have been other systems developed to achieve similar results by Carana Corporation financed by USAID and can be located on the Internet at: <http://www.carana.com>. Some of the international accounting firms have also devised profile by software systems to assist conversions of Russian accounting data into IFRS compliant financial statements.

In the Audit Expert and other software systems the financial data may be manually input in the initial forms of the specialized system for financial analysis, and as an alternative may be automatically "downloaded" from the general ledger. Thus, the Audit Expert system is equipped with a device that assures data exchange through commonly used Russian accounting software programs. Although a company uses software developed in-house, importing data into Audit Expert system is not a problem, since the data may be "downloaded" from the text file. Ability to import the data helps to avoid routine job and accomplish financial analysis within shorter period of time.

What are the conclusions that a manager of the company or a financial analysis specialist may make when applying managerial data and an IFRS conversion system? First of he or she may determine standard financial liquidity indicators, financial stability indicators, indicators of profitability and business operations of a company.

For example, the Audit Expert system creates a file with financial information of the company, performs by-item revaluation of assets and liabilities in the balance sheet, and, after that the system calculates financial indicators.

Financial ratios help to define weaknesses and threats in the movements of the financial condition of the company. Ready methods implemented in the Audit Expert system for financial analysis help to evaluate the liquidity risk, solvency and bankruptcy risk, to determine the return of equity risk and reserve for financial stability of the company.

In instances when balance sheet data and Income Statement data are not sufficient for base calculations, Audit Expert system is capable to incorporate additional information; such as data on allocation of profit, property information and debts.

In addition to the standard methods the conversion software systems should be designed to include methods that are primarily oriented at a separate group of users, however, they may be interesting for a wider group of people. Thus, banks are proactively using methods designed for analysis of financial condition of a borrower. State unitary institutions and joint-stock societies conduct financial analysis using methods governed by the regulatory requirements.

Conversion software systems should also help to forecast and determine the current financial condition of the company, and compare financial indicators of the company with industrial standards and regulatory requirements. This can be used as a "benchmark" for future plans development established in order to achieve the set objective of company's business.

### ***Financial indicators are the signs for success***

During implementation stage of the project, company management must have an understanding at any given moment of profitability of its business and efficiency of allocation of resources, stability of financial condition and future trends. The first adverse signs of the volatile condition may be identified long before they have a negative effect on a business.

Monitoring of prime indicators in the Audit Expert system may be performed on-line. Graphs and charts that require insignificant efforts shall reflect any changes in the key indicators, which help to make a judgement about "company's health condition". Even an inexperienced person will be able to analyze financial indicators and then make a right decision.

Using a good conversion software system like the Audit Expert a manager or specialist of the company should be able to build forecasts of the financial indicators. If this indicates the trend threatening the company's condition, then he/she may determine time for the critical points of financial indicators using the Forecast function.

*Marina Stupakova is a Pro-Invest-IT Manager. She can be contacted by e-mail: [stupakova@pro-invest.com](mailto:stupakova@pro-invest.com).*

## The Plekhanov Academy of Economics Starts ACCA Training Courses

**O**ne of the main aims of the present Accounting Reform in Russia is upgrading the professional qualification of accountants, financial analysts, auditors and other financial specialists.

Nowadays, a great number of foreign companies are operating in the Russian market and this, together with the process of globalisation and the creation of a united European market, places increasing demand on the requirement for specialists, qualified in international accounting standards.

As a result of this new trend there are more and more professional institutes offering specialist qualifications for Russian managers, particularly in the spheres of accountancy, finance, audit and marketing.

If personnel obtain one of the professional qualifications it guarantees that s/he is highly qualified modern specialist to international standards. This can significantly improve career advancement opportunities

One of the most popular professional Institutes is becoming increasingly well known in Russia - ACCA – the Association of Chartered Certified Accountants. It is a

non-commercial, international qualifications organization, which certifies financial specialists. It was founded in 1904 and its main office is in London. Currently it has nearly 300,000 students and members in 160 countries, which work in different spheres of commerce, government, education, industry and public services.

The Association already has its first representative office in Moscow and has more than 1000 students and about 300 members in Russia.

The ACCA operates over 200 examination centres in more than 140 countries. The ACCA currently uses British Council examination centres in Moscow, St. Petersburg and Vladivostok.

At the present time ACCA offers seven different certificates. One of the most popular certificates is the Chartered Certified Accountant (professional scheme). Those who achieve this certificate can use the logo ACCA and work in any sphere of finance. The ACCA programme includes 3 parts (14 examinations).

The ACCA was the first professional body to offer examinations based on international accounting standards (IAS). Students can choose from two main streams (International or UK) covering the following subjects: preparing financial statements, financial reporting, audit and internal review and advanced corporate reporting. In addition there are now Russian variants of the examinations in corporate and business law and business taxation, which will be of course more interesting and valuable for Russian students.

Students have ten years to complete all the examination

papers (starting from the date of their registration) but usually it takes no more than 3-4 years. There are two examination sessions per year – in June and December. Up to four subjects can be taken in one examination session, but subjects must be taken in order. In addition to completing the examinations successfully students are required to obtain a minimum of three years relevant practical experience in order to obtain the ACCA qualification.

From mid September to the end of November 2002 the International Business School at the Plekhanov Russian Academy of Economics will start professional training courses for the new ACCA syllabus examinations (December session). These courses will be run at weekends/evenings during a two-month period for the following subjects:

### **Part I**

- 1.1 Preparing financial statements;
- 1.2 Financial information for management;
- 1.3 Managing people

### **Part II**

- 2.1 Information systems;
- 2.2 Corporate and business law (Russia);
- 2.3 Business taxation (Russia);
- 2.4 Financial management and control;
- 2.5 Financial reporting;
- 2.6 Audit and internal review

All the ACCA exams are held in the English language, all lectures are in English as well (even Russian Tax and Russian Law).

*For more information please contact Alla Mitina (professional courses manager). She can be contacted by phone (095) 237 8517 or by e-mail: [develop@rea.ru](mailto:develop@rea.ru).*

## The International Center for Accounting Reform

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